

## Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-01  
INR-10 NSAE-00 ICA-20 XMB-04 OPIC-06 SP-02 LAB-04  
SIL-01 OMB-01 DODE-00 PA-02 /077 W  
-----081585 120427Z /21

R 111640Z SEP 78  
FM AMEMBASSY ROME  
TO SECSTATE WASHDC 5797  
TREAS DEPT WASH DC

UNCLAS ROME 16954

PASS FRB

E.O. 11652: N/A  
TAGS: EFIN, IT  
SUBJECT: IMF STANCE ON ITALIAN ECONOMIC SITUATION

1. SUMMARY. LAMBERTO DINI, EXECUTIVE DIRECTOR FOR ITALY IN THE INTERNATIONAL MONETARY FUND, STATED IN AN INTERVIEW IN CORRIERE DELLA SERA THAT IF THE ECONOMIC PROGRAM ADOPTED BY THE GOVERNMENT AND BY PARLIAMENT IS DEEMED TOO WEAK, THE FUND WOULD NOT BE DISPOSED TO CONCLUDE A NEW STAND-BY LOAN WITH ITALY. DINI SAID THERE WAS SUBSTANTIAL AGREEMENT BOTH WITHIN THE FUND AND BETWEEN THE FUND AND ITALIAN AUTHORITIES ON WHAT MEASURES SHOULD BE TAKEN TO PUT ITALY ON A HIGHER LONG-TERM NONINFLATIONARY GROWTH PATH, BUT THERE WAS ALSO EMERGING IN THE FUND A SCEPTICISM CONCERNING THE CAPACITY OF THE ITALIAN POLITICAL ORGANIZATION TO MAKE THE KINDS OF CHOICES SUCH MEASURES IMPLY, I.E. CUTS IN GOVERNMENTAL TRANSFERS AND SUBSIDIES. DINI MADE THE FOLLOWING POINTS IN THE INTERVIEW:

2. ON THE POSSIBILITY OF A NEW IMF-STANDBY LOAN. DINI SEES SUBSTANTIAL ACCORD ON THE NEED TO ALTER PUBLIC SPENDING PATTERNS, TO MODERATE COST OF LABOR INCREASES, AND TO ASSURE A BETTER UTILIZATION OF RESOURCES IN ORDER TO INCREASE EMPLOYMENT.

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THE PLAN RECENTLY PRESENTED BY TREASURY MINISTER PANDOLFI HAS NOT YET BEEN EXAMINED IN DETAIL BY THE FUND, BUT IF THE PROGRAM EVENTUALLY ADOPTED BY THE GOVERNMENT AND PARLIAMENT IS SEEN AS BEING TOO WEAK, THE FUND WOULD NOT SIGN A NEW STAND-BY. THERE ARE THOSE IN THE FUND THAT DO NOT EXPECT THE ITALIANS MAKE THE NECESSARY HARD CHOICES, GIVEN THE RECENT EASING OF BALANCE-OF-PAYMENTS PRESSURES.

3. ON THE NEED FOR A NEW STAND-BY. IT IS NOT LIKELY THAT ITALY WOULD HAVE TO DRAW ON A NEW STAND-BY LOAN IN THE IMMEDIATE FUTURE. BUT IT MUST BE EMPHASIZED THAT THE IMPROVEMENTS ON THE EXTERNAL SIDE AND IN PRICES HAVE BEEN MADE IN THE CONTEXT OF LOW GROWTH. THE ITALIAN ECONOMY IS AT PRESENT STALEMATED, WITH A LOW LEVEL OF INVESTMENT AND EMPLOYMENT AND THE HIGHEST INFLATION IN EUROPE. CERTAIN SECTORS OF IT'S INDUSTRY ARE EXPERIENCING FINANCIAL AND MARKET DIFFICULTIES, AND THERE IS ALWAYS THE POSSIBILITY OF A RAPID REVERSAL OF CAPITAL MOVEMENTS AND COMMERCIAL CREDIT. THERE IS THEREFORE SUFFICIENT UNCERTAINTY CONCERNING THE FUTURE COURSE OF THE ECONOMY AND THE BALANCE OF PAYMENTS THAT WOULD SEEM TO MAKE ADVISABLE THE NEGOTIATION OF A STAND-BY PROGRAM WITH THE FUND THAT WOULD ASSURE IT'S PARTNERS OF THE CORRECTNESS OF IT'S POLICIES, IMPROVE IT'S INTERNATIONAL CREDITWORTHINESS, AND INDIRECTLY REINFORCE THE LIRA ON THE EXCHANGE MARKETS.

4. WOULD A NEW STAND-BY PROGRAM BE DEFLATIONARY? CERTAINLY NOT IN THE SENSE OF RESTRICTING AGGREGATE DEMAND. IN THE FUND'S WORLD ECONOMIC OUTLOOK FOR THE NEXT 2 YEARS, ITALY IS ASSIGNED A GROWTH RATE OF 4 TO 5 PERCENT, WHICH IS CONSIDERED CONSISTENT WITH BALANCE-OF-PAYMENT EQUILIBRIUM, GIVEN THAT THE ITALIAN ECONOMY SEEMS TO HAVE ADJUSTED TO THE SHOCK OF THE OIL PRICE INCREASES. THE FUND SHARES THE JUDGEMENT THAT THE CURRENT INFLATION IS NOT CAUSED BY AN EXCESS OF AGGREGATE DEMAND, BUT BY THE RAPID UNCLASSIFIED

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INCREASE IN COSTS, ESPECIALLY LABOR COSTS RELATIVE TO PRODUCTIVITY, AND THAT CURRENT STAGNATION AND UNEMPLOYMENT ARE THE RESULT OF TOO LOW A LEVEL OF INVESTMENT AND THE LOW PRODUCTIVITY OF PUBLIC EXPENDITURES.

5. ON THE FUND'S INSISTENCE ON ITALIAN EXCHANGE RATE FLEXIBILITY, AS CONTAINED IN THE PRESENTER-OF-INTENT, AND THE PROPOSED NEW EUROPEAN MONETARY SYSTEM. THE RETURN TO MORE STABLE EXCHANGE RATES REQUIRES GREATER DISCIPLINE IN THE CONDUCT OF DOMESTIC ECONOMIC AND FINANCIAL POLICIES, ESPECIALLY IN THE COUNTRIES WITH HIGHER INFLATION, AND THE INTERNATIONAL COORDINATION OF THESE POLICIES. UNTIL THESE OBJECTIVES ARE ACHIEVED, HOWEVER, THE FUND'S ATTITUDE TOWARD THE FLEXIBILITY OF EXCHANGE RATES IS NOT LIKELY TO CHANGE.HOLMES

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## Message Attributes

**Automatic Decaptioning:** X  
**Capture Date:** 01 jan 1994  
**Channel Indicators:** n/a  
**Current Classification:** UNCLASSIFIED  
**Concepts:** ECONOMIC CONDITIONS, POLICIES, INTERNATIONAL ORGANIZATIONS  
**Control Number:** n/a  
**Copy:** SINGLE  
**Draft Date:** 11 sep 1978  
**Decaption Date:** 01 jan 1960  
**Decaption Note:**  
**Disposition Action:** n/a  
**Disposition Approved on Date:**  
**Disposition Case Number:** n/a  
**Disposition Comment:**  
**Disposition Date:** 01 jan 1960  
**Disposition Event:**  
**Disposition History:** n/a  
**Disposition Reason:**  
**Disposition Remarks:**  
**Document Number:** 1978ROME16954  
**Document Source:** CORE  
**Document Unique ID:** 00  
**Drafter:** n/a  
**Enclosure:** n/a  
**Executive Order:** N/A  
**Errors:** N/A  
**Expiration:**  
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**Review Release Event:** n/a  
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**Status:** NATIVE  
**Subject:** IMF STANCE ON ITALIAN ECONOMIC SITUATION  
**TAGS:** EFIN, IT, IMF  
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**Review Markings:**  
Sheryl P. Walter  
Declassified/Released  
US Department of State  
EO Systematic Review  
20 Mar 2014  
**Markings:** Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014